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IN THE

Supreme Court of the United States

OCTOBER TERM, 1933.

No. 78.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

TITLE GUARANTEE LOAN & TRUST COMPANY, AS TRUSTEE OF THE ESTATE OF J. H. WOODWARD.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

BRIEF FOR RESPONDENT.

OSCAR W. UNDERWOOD, JR.,
H. C. KILPATRICK,
Attorneys for Respondent.

E. J. SMYER,
Of Counsel.

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BRIEF FOR RESPONDENT.

OPINIONS BELOW.

The opinion of the United States Board of Tax Appeals (R. 42-49) is not officially reported. The opinion of the Circuit Court of Appeals (R. 66-68) is reported in 63 Fed. (2d) 621.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered February 17, 1933 (R. 68-69). The petition for a writ of certiorari was filed May 17, 1933, and was granted May 29, 1933. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED.

Whether a testamentary trustee is entitled to claim as a deduction, in computing the net income of the trust, the amount of the income of the trust for its taxable year which is to be distributed currently by the trustee to the testator's widow, one of the *cestuis que trustent* named in the will, where the widow, under the local law, had the right within a limited time to dissent from the will, but failed to exercise the right, and so took under the will.

STATUTES INVOLVED.

The statutes involved are set forth in the Appendix, *infra*, pp. 16, 17.

STATEMENT.

To the summary of the facts, set out on pages 2 and 3 of petitioner's brief herein, we add the following:

The trust property was devised to the trustee in trust, and delivered to the trustee in the year 1919 (R. 45). By the terms of the trust, the trustee was authorized and directed to pay from income all cost and expense incident to the preservation and protection of the trust estate, and: "All the rest and residue of the net income from the trust estate, I direct the trustee to pay over *as and when received,* share and share alike to my wife, Martha Woodward, my son Alan H. Woodward, my daughter, Bertha W. Underwood, and my daughter, Margaret W. Hopkins, or the

survivors of them." There is no mention of dower or statutory interest anywhere in the trust or will, and no reference thereto.

The trust is to terminate on the death of the survivor of the three children. On the termination of the trust, the trustee is directed to divide the trust property share and share alike between the grandchildren of testator then living, the descendant of a deceased grandchild taking the share which the parent would have taken if living. (R. 43, 44.)

The widow, Martha B. Woodward, died May 13, 1928 (R. 45). The decision in the *Bolster* case was handed down one month after the death of the widow. (R. 47.) 26 Fed. (2d) 760.

From the time the trust property came into the custody of the trustee, in 1919, to May 13, 1928, the date of death of the widow, distribution was made to the widow by the trustee currently "as and when received" in the amount of her distributive share of the net income. (R. 45.) For the taxable years 1919 to 1928, both inclusive, the trustee filed fiduciary returns with the Collector, and in computing the taxable income of the trust estate, deducted from gross income the amount so distributed to all of the beneficiaries in accordance with the terms of the trust. The petitioner allowed these deductions without question until February 26, 1929, when he denied respondent the right to deduct amounts distributable to the widow for the years 1924 to 1927 inclusive (R. 15-21), and on October 15, 1930, he denied a similar deduction for 1928 (R. 37-40). Martha B. Woodward made and filed with the Collector an individual income tax return for each of the taxable years 1919 to 1927, both inclusive, and in each return included the amount which had been distributed to her during the taxable year, and paid income tax thereon. (R. 47.) The taxes so paid for the years 1923 to 1927, inclusive, were refunded to her executor in 1930 (R. 47-48).

SUMMARY OF ARGUMENT.

I.

The statute permits, unconditionally and without exception, the deduction by the fiduciary of the amount of the income of the trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries. The statute contains no express exception or limitation, nor does it contain language which can be construed as supplying such an exception or limitation.

II.

The testator's widow was a "beneficiary" of the trust of which respondent was the trustee or fiduciary, so the amount of the trust income distributable currently to her was deductible in computing the net income of the trust. The term "beneficiary" is synonymous with the term "*cestui que trust*". This well established meaning, recognized for years by the executive and ratified by repeated reenactments of Congress, may not be disturbed. Neither the non-taxability of the widow nor the theory that she is a purchaser can alter the meaning of the term.

ARGUMENT.

This and the companion cases, Nos. 75, 76 and 77, involve similar questions, except for the fact that in No. 77, *Helvering v. Pardee,* the widow was given a fixed annuity under her husband's will, whereas in this case and in Nos. 75 and 76 the widow was to receive distributions only from the income, if any, of the trust.

I.

The statute permits, unconditionally and without exception, the deduction by the fiduciary of the amount of the income of the trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries.

The pertinent provisions of the statute here under consideration are these, appearing in Section 219 (b) of the Revenue Acts of 1924 and 1926, and being in substance the same as Section 162 (b) of the 1928 Act:

> "* * * The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in Section 212, except that—
>
> * * * * * * *
>
> "(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, * * * but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. * * *"

The terms of this statute are clear, and when the terms of a statute are clear they must be enforced.

The will directed that the income should be distributed "as and when received" to the widow and the children (Pet. brief p. 2; R. 43), in other words, "currently". Therefore, so far as the trustee is concerned, it, the trustee, under the plain and unambiguous terms of the law, is entitled to the deduction.

The statement in the statute that the amount allowed as a deduction shall be included in computing the net income of the beneficiaries "whether distributed to them or not" is something which relates to the beneficiaries, not to the trustee; and, after examining the petitioner's contentions, we shall show that Congress included that clause to make

the income taxable to the beneficiaries, if taxable at all, in the same year for which it is deducted by the trustee upon its fiduciary return (pp. 8, 9).

Now, let us examine the petitioner's contentions: The petitioner, while admitting on the one hand that the widow here was a "beneficiary" and denying it on the other hand (a position hereafter discussed at p. 11) contends that the right to the deduction is "only on the condition that the liability to the tax is transferred with the payments." This conclusion is based upon the following reasoning:

1. That there is manifest in the statute an intention on the part of Congress to tax all income of trust estates, which intention should not be thwarted by the Court;

2. That since, under decisions cited, the widow was not subject to tax on the distributions here in question, to allow the trustee the deduction would be to permit the income to escape taxation with the result that an *exemption* would be established "by inference or presumption", which is not permissible;

3. That the only course left open to the Court is to construe the statute as permitting the deduction only upon condition the amount deducted shall be taxed to the distributee.

We answer these propositions as follows:

1. This Court may not enforce a general intention to tax all incomes unless that intention "be carried into language which can reasonably be construed to effect it." See *Smietanka v. First Trust and Savings Bank,* 257 U. S. 602, 605, 606, 66 L. ed. 391, 393, where a collector contended that income accumulated by a trustee for unborn and unascertained beneficiaries should be taxed, under an alleged general intention of Congress to tax all incomes.

Nothing is better settled than that, in the construction of a law, its meaning must first be sought in the language employed. If that be plain, it is the duty of the courts to enforce the law as written. *United States v. Standard Brewery,* 251 U. S. 210, 217, 64 L. ed. 229, 243. The literal

meaning of the words employed is most important, for taxing statutes are not to be extended by implication beyond the clear import of the language used. If the words are doubtful, the doubt must be resolved in favor of the taxpayer, *United States v. Merriam*, 263 U. S. 179, 187, 188, 68 L. ed. 240, 244. *United States v. Field*, 255 U. S. 257, 262, 65 L. ed. 618, 620.

2. The question here presented is the right of the trustee to a *deduction* in computing net income. The question of the *exemption* of that income from taxation is not involved. The rule, cited by the petitioner, that nothing is to be taken by inference or presumption in favor of an exemption, has no application in the determination of the right to a deduction from gross income in computing the net income. A liberal construction is given to words of *exception* confining the operation of a tax, though the rule regarding *exemptions* may be different. *Eidman v. Martinez*, 184 U. S. 578, 583, 46 L. ed. 697, 701. Though the petitioner repeatedly insists that a question of *exemption* is involved here, a glance at the statute will show that nothing in the nature of an exemption was mentioned or contemplated.

3. While carefully refraining from an assertion that Section 219 (b) (2) contains an express limitation upon the trustee's right to deduct income distributions to beneficiaries, the petitioner repeatedly asserts that the deduction is limited to amounts which are taxable in the hands of the beneficiary. By inference, petitioner supports this position by citing that clause of the statute which provides: "but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not." But the statute does not say that the trustee may take the deduction "on condition" or "provided," or "if" the amount deducted is included in computing the beneficiary's income. Congress might have used such terms had it wished, although it is

likely that Congress, if it had the intention attributed to it by the petitioner, would have made its meaning entirely clear through an outright statement that the trustee might have the deduction if the beneficiary should pay tax upon the amount distributed.*

Congress did not intend to attach a condition to the allowance of the deduction. On the contrary, we assert confidently that it is evident, from an examination of the statute as a whole, that the clause in question was inserted in the statute for the sole and only purpose of providing that the income should be taxable to the beneficiary *in the same taxable year in which it should be deductible by the trustee.*

Section 213 (a) of the 1924 (26 U. S. C. A. § 954; c. 234, 43 Stat. 267) and 1926 (c. 27, 44 Stat. 23) Revenue Acts, and Section 22 (a) of the 1928 Act (c. 852, 45 Stat. 797), provided that gross income should include "gains, profits, and income derived from * * * dealings in property * * * growing out of the ownership * * * of or interest in such property; also from interest, rent, dividends, securities * * * or gains or profits and income derived from any source whatever"; and also Section 213 (a) of the 1924 and 1926 Acts, and Section 42 (c. 852, 45 Stat. 805) of the 1928 Act, provided that the amount of all such items "shall be included in the gross income for the taxable year *in which received by the taxpayer,*" with an exception in the case of a taxpayer whose books should be kept on a different basis. Under these provisions the taxability of an individual recipient of income was established, although the time of taxability was made to depend upon the time of receipt in the case of one reporting on the basis of cash receipts. Without further specific provision, therefore, the beneficiary might be taxable upon the trust income in a year subsequent to that in which the fiduciary might take the deduction, since the fiduciary was allowed to deduct the

*The trustee's failure to take advantage of a statutory deduction does not give the beneficiary a right to the same. *Riker v. Com'r.*, 42 Fed. (2d) 150, *Little v. White*, 47 Fed. (2d) 512.

amount "which is to be distributed", and was not limited to actual distributions within the year of deduction. It was to meet this incongruous situation that the language upon which the government now relies was inserted in Section 219. The important provision in that clause is the phrase "whether distributed to them or not." By the use of this language it was made plain that the beneficiary of a trust estate should return distributable trust income for the year in which the fiduciary was allowed the deduction, and could not postpone the return thereof until actual receipt, as he could otherwise have done under Section 213 (a).

The absurd consequences which would result from reading into the statute the condition proposed by the petitioner are apparent. The fiduciary, in every case, would be required, at his peril, to determine whether or not the distribution would be taxable to the beneficiary.† This might indeed be a heavy burden when it is considered that pre-existing relations between the creator of the trust and the beneficiary, the character of the beneficiary, the statutory exemptions or deductions allowed the beneficiary, or some other fact or circumstance might affect the taxability of part or all of the distribution in the hands of the beneficiary. Under this construction, a prudent trustee might be forced in effect to interplead the government and the beneficiary and call upon the courts for a determination, in each instance, of the extent of the beneficiary's tax liability as a prerequisite to the determination of the trustee's right to a statutory deduction.

† In fact, the petitioner seems to argue (p. 25 of brief in No. 75) that the fiduciary may take the deduction only if the beneficiary "does in fact pay the tax"; that is, even if the distribution be *taxable* to the beneficiary, the fiduciary may not take the deduction if the fiduciary *fails to pay* the tax. In other words, petitioner would make the fiduciary's right to the deduction depend upon the beneficiary's failure or refusal, perhaps long after the distribution, to perform an act which the trustee is powerless to require.

II.

The testator's widow was a beneficiary of the trust.

The petitioner contends that the widow was not a "beneficiary" of the trust established by the will of J. H. Woodward. By that will, the decedent devised and bequeathed his residuary estate to respondent in trust, the net income therefrom, after payment of a small monthly annuity to a named beneficiary, to be paid over, as and when received, to the testator's widow and his three children, in equal shares (R. 23).

In *Reinecke v. Smith* (decided April 10, 1933), 289 U. S. 172, 77 L. ed. 692, 693, it was argued by the respondent that the term "beneficiary", as used in subdivision (g) of Section 219 of the Revenue Act of 1924, included the trustee. Subdivision (b) of the same section is before the Court in the instant case. There is nothing in the statute to indicate that Congress intended to use the term in different senses in these two subdivisions, but on the contrary, they both have to do with the taxation of "the income of estates or of any kind of property held in trust" (see subdivision (a) of the same section). It must be presumed therefore, that the term is used in the same sense in both subdivisions. *Pampanga Mills v. Trinidad*, 279 U. S. 211, 73 L. ed. 665.

In the *Reinecke* case, the argument that the trustee was a beneficiary was rejected by this Court in the following language:

> "The unambiguous phraseology of the Act precludes the suggested construction. A trustee is not subsumed under the designation beneficiary. Both words have a common and accepted meaning; the former signifies the person who holds title to the *res* and administers it for the benefit of others; the latter the *cestui que trust* who enjoys the advantages of such administration. The ordinary meaning of the terms used, which we are bound to adopt (Old Colony R. Co. v. Commissioner of Internal Revenue, 284 U. S. 552, 560, 76 L. ed. 484, 489, 52 S. Ct. 211), and the view held by those charged

with the enforcement of the Act, ratified by re-enactment of the section, alike forbid the adoption of the construction for which the respondents contend."

The definitions of "trustee" and "beneficiary" thus stated are those accepted by common understanding and universally by the courts. It must be presumed that Congress used the terms in the same sense. *United States v. Merriam,* 263 U. S. 179, 187, 68 L. ed. 240, 244.

The petitioner, however, urges that the common and accepted meaning of the term "beneficiary" should not be adopted in construing Section 219 (b) (2) of the 1924 and 1926 Acts and the corresponding provision of the 1928 Act, but that the term "beneficiaries" should be applied only to those distributees of trust income who are taxable on *distributions received.* Contending with one breath that the widow in the instant case was so taxable, and with the next that she was not, petitioner does not unequivocally place her within or without the term "beneficiaries", but seems to argue that if she is not taxable, she is not a beneficiary, and that, only on that theory, the trustee is not entitled to the deduction. This novel contention is no doubt derived from the perplexing position in which the petitioner, as an administrative officer, finds himself, and of which he is at pains to explain to the Court. The petitioner attempts to support his position by the statement that this Court has already adopted the construction contended for in *Burnet v. Whitehouse,* 283 U. S. 148, 75 L. ed. 917. In that case it was held that an annuity payable from corpus and regardless of income, constituted a bequest. In holding that Section 219 does not make the payments taxable, the Court pointed out that Section 219 applied only to income of the trust, paid as such to a beneficiary, and that the annuity payments there involved were payable regardless of whether they were from income or corpus. Since the terms of the will in the instant case permit distributions only from income of the trust estate

and since the distributions here were distributions "of income paid as such to a beneficiary," the *Whitehouse* decision supports our position, rather than petitioner's, and certainly it is not authority for ignoring the well-settled meaning of the term "beneficiaries."

The petitioner asserts that the court below erroneously gave the word "beneficiaries" its "most comprehensive meaning." While we contend that the word, as used in the law of trusts, has only one meaning, the "comprehensive" meaning in question, we submit that, if there were any doubt as to its meaning, that doubt should be resolved in favor of the construction for which we contend, not only because doubts must be resolved against the government, but also by reason of the long established executive construction given to the statute. The statutory provision here under consideration was re-enacted without substantial change in all of the revenue acts subsequent to the 1924 Act. (See Sec. 219, Rev. Act of 1926, and Sec. 162, Rev. Acts of 1928 and 1932.) In Regulations 65, Art. 347 (see appendix, p. 17), construing subdivisions (g) and (h) of Section 219 of the 1924 Act, the Commissioner of Internal Revenue defined the term "beneficiary", as including "any person entitled to an interest in the income or the principal of a trust." By its subsequent re-enactments, Congress impliedly approved the construction given in the regulations which the Commissioner had followed since 1918, and it was not until 1929 that the Commissioner attempted to give the narrow meaning now urged by him. Congress is presumed to have legislated with the knowledge of the established custom or usage of the executive department.

Old Colony R. R. Co. v. Com'r., 284 U. S. 552, 76 L. ed. 484.
Nat'l Lead Co. v. United States, 252 U. S. 140, 64 L. ed. 496.

The ordinary meaning of the term "beneficiaries", and the view held for so many years by those charged with the

enforcement of the Act, ratified by re-enactment of the section, alike forbid the adoption of the construction for which the petitioner contends. *Reinecke v. Smith, supra.*

Apparently realizing the difficulties inherent in his argument that the "beneficiaries" mentioned in the statute are only those distributees who are taxable or who pay tax upon distributions received, petitioner falls back upon the theory upon which these cases were decided by the Board of Tax Appeals, namely, that, since the distributions to the widow constituted a return of capital to her, they were not distributions of trust income *as such* to her, and therefore are not covered by the terms of Section 219 (b) (2). True, petitioner argues that the distributions were income in her hands and not a return of capital, but he urges this Court to review that question and decide first whether such distributions did constitute a return of capital, and if so, to deny the respondent's right to the deduction.

In the instant case, the Circuit Court of Appeals repudiates the so-called return of capital theory, and holds that the distributions to the widow represented taxable income to her, as did the New York Court of Appeals in *People ex rel. Kight v. Lynch,* 255 N. Y. 323. The Circuit Court of Appeals for the Third Circuit in the companion cases, Nos. 75, 76 and 77, refused to decide the question of the taxability of the widow and based its decision upon the plain words of Section 219. Under the law of Alabama, a widow who takes under the will in lieu of dower is not a creditor of the estate. Although she is preferred over other beneficiaries, the creditors' rights have priority over hers. *Steele v. Steele,* 64 Ala. 438.

Clearly, the respondent here could and did distribute nothing but income of the trust, and we submit that, whether that income was taxable income or non-taxable in the hands of the widow, Section 219 permits the fiduciary to deduct it, and it is a clear perversion of the theory of the return of capital to hold that, because of that theory, the widow was not a beneficiary. A similar contention was

considered and rejected in *Orton v. Orton,* 42 N. Y. (3 Keyes) 486, cited with approval in *United States v. Merriam,* 263 U. S. 179, 184, 68 L. ed. 240, 243. In the *Orton* case, the legacy was given in lieu of dower, and a provision was made that, should there be a surplus after the payment of specific legacies, the legatees should share proportionately therein. The executor contended that the widow was not entitled to share in the surplus, *because a bequest in lieu of dower was not a legacy;* in other words, that the widow did not take as a legatee, but as a purchaser for value. However, the Court held, notwithstanding the bequest was declared by the will to be in lieu of dower, that it was still a legacy. The Court said:

> "Every bequest of personal property is a legacy, including as well those made in lieu of dower and in satisfaction of an indebtedness as those which are wholly gratuities. The circumstance whether gratuitous or not does not enter into consideration in the definition."

This language was adopted by this Court in *United States v. Merriam, supra,* where it was held that bequests in lieu of compensation for acting as such, were exempt from taxation, as bequests in the hands of the executors. It was there unsuccessfully argued that the term "bequest" implied a bounty or gratuity.

In *Gruver v. Wood,* 174 Mass. 540, it was held that a widow who took a bequest in lieu of dower was nevertheless a "beneficiary under the will."

If the terms "legacy", "bequest", and "beneficiary" in the law of wills do not depend upon the circumstance of being gratuitous, clearly the term "beneficiary of a trust" has no reference to such a circumstance. The interest of a beneficiary under a trust may be acquired by purchase, by testamentary disposition, or by gift *inter vivos. Butterworth v. Commissioner,* 63 Fed. (2d) 944, 947. This is fundamental law, presumably known to Congress when it used the term in the statute.

CONCLUSION.

The judgment of the Circuit Court of Appeals should be affirmed, whether this Court considers the distributions to the widow as taxable income to her or not.

Respectfully submitted,

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Of Counsel.

APPENDIX.

Statutes Involved.

Revenue Act of 1924, c. 234, 43 Stat. 253, 275:

SEC. 219 (a) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—

* * * * * * *

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, * * *

* * * * * * *

(b) Except as otherwise provided * * * the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that—

* * * * * * *

(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, * * * but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. * * * (26 U. S. C. A. § 960.)

Section 219 of the Revenue Act of 1926, c. 27, 44 Stat. 9, 32, is identical with Section 219 of the Revenue Act of 1924, *supra*. Sections 161 and 162 of the Revenue Act of 1928, c. 852, 45 Stat. 791, 838, are substantially the same as Section 219 of the Revenue Acts of 1924 and 1926. Section 162 (b) of the Revenue Act of 1928 repeats, without material change, the provisions of Section 219 (b) (2) of the earlier Acts.

The following Sections of the Code of Alabama of 1907 were in effect from the time that the respondent entered upon its duties as trustee in 1919, being re-enacted in the Code of 1923 under the section numbers shown in parentheses:

SEC. 3812 (7427) *Dower Defined;* * * * Dower is an estate for the life of the widow in a certain portion of the following real estate of her husband, to which she has not relinquished her right during the marriage; * * *

SEC. 3813 (7428) *Extent of widow's dower interest.* The quantity of the dower interest is as follows:

(1) When the husband dies leaving no lineal descendants and his estate is not insolvent, a widow is entitled to be endowed of one-half his lands. * * *

(3) When there are lineal descendants, then to one-third part thereof, whether the estate be solvent or not.

SEC. 6168 (10593) *Dissent by widow; her rights on;* * * * The widow may, in all cases, dissent from the will of her deceased husband, and, in lieu of the provision made for her by such will, take her dower in the lands and such portion of the personal estate as she would have been entitled to in case to intestacy. * * *

SEC. 6169 (10594) *Dissent; when to be made.*—Such dissent must be made in writing and deposited within twelve months from the probate of the will with the judge of probate of the county in which the will is probated, and an entry must be made of record specifying the day on which the dissent was made. * * *

Treasury Regulations.

Article 347 of Treasury Regulations 65 construing Section 219 of the Revenue Act of 1924, provided in part as follows:

> The term "beneficiary" as used in this article includes any person entitled to an interest in the income or the principal of a trust, but does not include one having merely a nominal interest in the income or principal.

This definition was brought forward in Regulations 69, Article 347, construing Section 219 of the Revenue Act of 1926, and in Regulations 74, Article 881, construing Section 161 of the Revenue Act of 1928.